

BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

OCTOBER 21, 2004

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In re: Joint Application of)
)
GE BUSINESS PRODUCTIVITY SOLUTIONS, INC.)
)
and)
)
BUSINESS PRODUCTIVITY SOLUTIONS, INC.)
)
)
For Expedited Approval of (i) the Transfer of)
Assets, Including the Customer Base, of)
GE Business Productivity Solutions, Inc. to)
Business Productivity Solutions, Inc.; (ii) the Transfer)
of GE Business Productivity Solutions, Inc.'s)
Operating Authority in Tennessee to)
Business Productivity Solutions, Inc.; and)
(iii) GE Business Productivity Solutions, Inc.'s)
Discontinuance of Service in Tennessee)

Docket No. 04-00370

APPLICATION AND REQUEST FOR EXPEDITED TREATMENT

GE Business Productivity Solutions, Inc. ("GEBPS") and Business Productivity Solutions, Inc. ("BPS") (together, "Applicants"), through their undersigned counsel and pursuant to T.C.A. § 65-4-113, hereby respectfully request that the Tennessee Regulatory Authority ("Authority" or "TRA") grant them authority to consummate a transaction involving the transfer of substantially all of the assets of GEBPS, including GEBPS's customer base and certificate of convenience and necessity, to BPS without interruption of service. Pursuant to the terms of an Asset Purchase Agreement ("Agreement") dated October 13, 2004, as described in more detail below, BPS's ultimate parent company, Eschelon Telecom, Inc. ("ETI"), will acquire

substantially all of the assets of GEBPS, including the GEBPS customer base and, where necessary, state telecommunications authorizations, including GEBPS's authorization in Tennessee, and immediately transfer these assets to BPS (the "Transaction"). Accordingly, Applicants request that the Authority approve the transfer of the customers of GEBPS to BPS. BPS currently is not authorized to provide telecommunications services in Tennessee. Thus, Applicants request that the TRA approve the transfer of the telecommunications authorization of GEBPS in Tennessee to BPS so that BPS can provide service to the existing customers of GEBPS. The existing tariff of GEBPS will be re-filed with the name BPS so that customers will continue to receive their same services at the same rates, terms and conditions.

After consummation of the Transaction, including the transfer of all of the GEBPS customers to BPS, GEBPS will no longer offer telecommunications services in Tennessee, and, therefore, GEBPS requests authority to discontinue the provision of telecommunications services effective as of the date of the customer transfer. The proposed Transaction is not expected to result in any loss or impairment of service to any of the customers of GEBPS. Customers will continue to receive their existing services at the same rates, terms and conditions and any future changes in the rates, terms and conditions of service will be made consistent with TRA requirements. The only change will be in the customers' service provider.

The Applicants respectfully request *expedited* treatment and consideration of this Application so that the Applicants' business plans can be implemented—the Applicants' business plans include consummation of the Transaction on or about *December 31, 2004*.¹ Thus,

¹ In order to ensure that the GEBPS customers continue to receive high quality services pending closing, Eschelon (as that term is defined hereinafter) or one of its subsidiaries may, should it be necessary and under certain conditions, provide certain management and related services to GEBPS on an interim basis until all required regulatory approvals and consents are received. BPS would provide any such services on behalf of GEBPS.

Applicants respectfully request that the Authority grant all relief sought herein on or before December 31, 2004.

In support of this Application, Applicants respectfully provide the following information:

I. APPLICANTS

A. GE Business Productivity Solutions, Inc.

GEBPS is a Georgia corporation. GEBPS is a direct, wholly owned subsidiary of General Electric Capital Corporation, which is a direct, wholly owned subsidiary of General Electric Capital Services, Inc., which is a direct, wholly owned subsidiary of the ultimate parent corporation, General Electric Company ("GE"), a New York corporation headquartered at 3135 Easton Turnpike, Fairfield, Connecticut 06431. GE is a widely held public corporation, and one of the largest and most diversified industrial corporations in the world. GEBPS is authorized to provide resold long distance telecommunications services virtually nationwide, including in Tennessee.² In Tennessee, GEBPS is authorized to provide local and long distance resale services. GEBPS also holds Section 214 authorizations from the Federal Communications Commission to provide domestic and international resold switched services. After consummation of the Transaction, all of GEBPS's customers will have been transferred to BPS. In addition, GEBPS will cease providing telecommunications services and will no longer require its authorization to provide telecommunications services in Tennessee.³

and subject to GEBPS's direction and control in a manner consistent with the certificates and tariffs of GEBPS, and applicable law and regulations.

² The TRA authorized GEBPS to provide local and long distance resale services on October 15, 1996 in Docket No. 96-01430.

³ GE has two other subsidiary telecommunications companies, Advanced TelCom, Inc. ("ATI") and Shared Communications Services, Inc. ("SCS"). ATI and SCS are not authorized to provide telecommunications services in Tennessee. However, simultaneously with the signing of the Agreement, the parent company of ATI and SCS,

B. Business Productivity Solutions, Inc.

BPS, a newly formed Minnesota corporation incorporated on October 7, 2004, is located at 730 2nd Avenue South, Suite 900, Minneapolis, Minnesota 55402, (612) 376-4400 (telephone), (612) 436-6816 (facsimile). BPS is a direct, wholly owned subsidiary of Eschelon Operating Company ("OPCO"), a Minnesota corporation, which in turn is a direct, wholly owned subsidiary of ETI, a Delaware corporation, the ultimate parent corporation. OPCO has several direct, wholly owned subsidiaries that offer telecommunications services in various states.⁴ ETI and its subsidiaries, collectively "Eschelon", all headquartered at the above address, provide voice, data, Internet services and business telephone systems to over 38,000 customers and have over 225,000 access lines⁵ in service. Eschelon provides local and long distance facilities-based service in 12 markets in 7 states.

As noted above, BPS is applying for authority to acquire GEBPS's telecommunications authorization in Tennessee so that it can acquire the existing customers of GEBPS. As one of the fastest growing telecommunications companies in the nation, currently providing service in 7 states, Eschelon has the financial, managerial and technical qualifications needed to provide quality telecommunications services to customers in Tennessee, as described further below. BPS's Articles of Incorporation are appended hereto as *Exhibit A*. BPS currently is in the process of becoming authorized to transact business in Tennessee as a foreign corporation, but it

Advanced TelCom Group, Inc. ("ATGI"), and ETI signed a Stock Purchase Agreement whereby ETI will acquire all of the issued and outstanding shares of common stock of ATI, and thereby, SCS. Thus, the Transaction is part of a larger transaction whereby ETI is acquiring ATI.

⁴ Eschelon Telecom of Minnesota, Inc., Eschelon Telecom of Washington, Inc., Eschelon Telecom of Colorado, Inc., Eschelon Telecom of Nevada, Inc., Eschelon Telecom of Arizona, Inc., Eschelon Telecom of Utah, Inc. and Eschelon Telecom of Oregon, Inc.

is not licensed to provide telecommunications services in any state at this time. Applicants will late-file the appropriate documentation from the Tennessee Secretary of State showing BPS's authorization to transact business in Tennessee.

An organizational chart showing the corporate structure of Eschelon upon completion of the Transaction is appended hereto as *Exhibit B*.

II. DESIGNATED CONTACTS

The designated contacts for this Application are:

Henry M. Walker, Esq.
Boulton Cummings Connors Berry, PLC
414 Union Street, Suite 1600
P.O. Box 198062
Nashville, Tennessee 37219
(615) 252-2330 (telephone)
(615) 252-6330 (facsimile)

Brad E. Mutschelknaus, Esq.
Melissa S. Conway, Esq.
KELLEY DRYE & WARREN LLP
1200 19th Street, N.W., Fifth Floor
Washington, D.C. 20036
(202) 955-9600 (telephone)
(202) 955-9792 (facsimile)

with copies to:

Victor A. Allums
Meredith H. Gifford
GE BUSINESS PRODUCTIVITY SOLUTIONS, INC.
3225 Cumberland Boulevard, Suite 920
Atlanta, Georgia 30339
(770) 541-5781 (Victor Allums telephone)
(770) 541-5782 (Meredith Gifford telephone)
(770) 541-5703 (facsimile)

J. Jeffery Oxley
ESCHELON TELECOM, INC.
730 2nd Avenue, South, Suite 900
Minneapolis, MN 55402
(612) 436-6692 (telephone)
(612) 436-6792 (facsimile)

⁵ Eschelon defines "access lines" as 64kbps channels. Consequently, for example, a T-1 line will be counted as multiple access lines depending upon the number of 64kbps channels established on the circuit.

III. THE TRANSACTION AND TRANSFER OF CUSTOMERS

On October 13, 2004, GEBPS and ETI signed the Agreement providing for ETI's acquisition of substantially all of the assets of GEBPS, including the GEBPS customers, which are to be transferred immediately to BPS. The proposed transfer of customers from GEBPS to BPS will have no adverse impact on customers. Following completion of the Transaction, BPS will provide resold long distance telecommunications services to the former customers of GEBPS. The GEBPS customers will continue to receive their existing services at the same rates, terms and conditions that they have prior to the transfer and any future changes in the rates, terms and conditions of service will be made consistent with Authority requirements.

To ensure a seamless transition and avoid customer confusion or inconvenience, Applicants will provide advance written notice to the affected customers at least thirty (30) days prior to the transfer, explaining the change in service provider in accordance with applicable Federal Communications Commission and state requirements for changing a customer's presubscribed carrier. A copy of the notification letter that will be sent to the affected customers is appended hereto as *Exhibit C*.

IV. QUALIFICATIONS OF BPS

The Applicants respectfully request that the TRA approve the transfer of GEBPS's existing telecommunications authorization in Tennessee to BPS. As noted above, GEBPS is authorized to provide local and long distance resale services pursuant to the authorization granted by the Authority on October 15, 1996, in Docket No 96-01430. As BPS is not currently certified in this state, the transfer of GEBPS's authority to BPS is necessary to enable BPS to begin providing service to GEBPS's existing customers as part of the Transaction. Appended hereto as *Exhibit A*, is a copy of BPS's Articles of Incorporation. As noted above, BPS is in the

process of obtaining its qualification to transact business in Tennessee as a foreign corporation and will late-file a copy of this documentation upon receipt. As demonstrated below, BPS has the requisite financial, managerial, and technical competence to provide telecommunications service in Tennessee and grant of the proposed transfer of GEBPS's operating authority is in the public interest.

A. Financial Qualification

BPS is financially qualified to provide telecommunications services in Tennessee. BPS, with the financial backing of its ultimate parent company, ETI, has access to the financing and capital necessary to conduct its telecommunications operations and to fulfill any obligations it may undertake with respect to the operation and maintenance of its services. Submitted herewith as *Exhibit D*, is ETI's SEC Form 10-Q for the quarterly period ended June 30, 2004, which includes consolidated balance sheets for December 31, 2003 and June 30, 2004, consolidated statements of operations for the three months and six months ended June 30, 2004, consolidated statements of cash flows for the six months ended June 30, 2003 and 2004, and notes to the consolidated statements. ETI is a privately-held company, but because of a recent bond issue, ETI is a public reporting company with filing obligations with the SEC. As noted in the 10-Q, ETI has increased its annual revenue from \$41.7 million for the year ended December 31, 1999 to \$141.1 million for the year ended December 31, 2003, and increased gross profits from \$14.8 million to \$80.3 million over the same period. ETI has been cash-flow positive three out of four quarters since September 2003 and is EBITDA positive in all of its markets. Clearly, ETI is financially qualified to provide quality telecommunications services to customers in Tennessee.

B. Managerial and Technical Qualification

BPS has the requisite technical and managerial qualifications to provide telecommunications services in Tennessee. As noted above, Eschelon already is authorized to provide telecommunications services in 7 states, and provides voice, data, Internet services and business telephone systems to over 38,000 customers and has over 225,000 access lines in service. Eschelon has successfully provided a host of local and long distance telecommunications services over the past several years. Eschelon operates a reliable and diverse voice and data network using proven technology by leading manufacturers which includes: transport diversity to ensure the highest level of network reliability; local and centralized technical resources; and 24 by 7 network monitoring. Both sales and service personnel are trained professionals. For customer inquiries, the toll-free customer service number will be 1-800-285-6100, after consummation of the Transaction. Eschelon has an experienced management team with more than 100 years of combined telecommunications experience. As the resumes appended hereto as *Exhibit E* show, Eschelon's management team possesses significant experience in successfully running a telecommunications business. Collectively, members of Eschelon's management team have designed, managed, and/or operated advanced telecommunications facilities throughout the United States. These already formidable capabilities will be augmented by the facilities and personnel obtained in the Transaction.

V. ADOPTION OF GEBPS'S EXISTING TARIFF

In connection with the transfer of GEBPS's authorization to BPS, the Applicants also request that BPS be allowed to adopt GEBPS's existing tariff, subject only to a minor name change to reflect the new name of the issuing carrier, BPS. None of the rates, terms, and

conditions in GEBPS's existing tariff will change at this time. The Applicants respectfully request that the tariff be allowed to take effect at the time of the customer transfer to BPS, in order to avoid any gap in service to customers. This way, existing GEBPS customers will continue to receive the same services at the same rates, terms and conditions as at present.

VI. DISCONTINUANCE OF SERVICE OF GEBPS

As noted previously, upon completion of the Transaction, GEBPS will no longer be offering telecommunications services in Tennessee. GEBPS, therefore, requests that the TRA grant it authority to discontinue service upon the transfer of its customers to BPS. The Applicants are complying with the Authority's regulations relating to the transfer of a customer base and, as noted above, will provide notice of the transfer of service to the affected GEBPS customers at least 30 days prior to the transfer. A copy of the notification letter is appended hereto as *Exhibit C*.

VII. PUBLIC INTEREST CONSIDERATIONS AND REQUEST FOR EXPEDITED PROCESSING

The Applicants submit that the Transaction is in the public interest. It is expected that the Transaction will increase competition in the Tennessee telecommunications market by strengthening Eschelon's position as an effective and multifaceted telecommunications carrier. As noted above, the Transaction is part of a larger transaction whereby ETI, BPS's ultimate parent company, will acquire ownership and control of two GEBPS affiliates, ATI and SCS. ETI's acquisition of these operating subsidiaries of GE, including the customer base of GEBPS, will allow Eschelon to combine its financial, technical and market resources and expertise with that of ATI, SCS and GEBPS, thereby enhancing its ability to provide reliable, competitively priced services to customers in Tennessee. The public interest benefits applicable to ETI's

acquisition of ATI and SCS, GEBPS's affiliates, will benefit the existing GEBPS customers as they will be joining a stronger Eschelon family of companies, all of which are focused exclusively on telecommunications services.

The Applicants emphasize that, following the transfer, the former GEBPS customers will continue to receive services from an experienced and qualified carrier, whose services will be consistent with the quality of services currently provided by GEBPS. GEBPS provides Centrex-based service to its business customers and Eschelon has many years of experience supporting Centrex. GEBPS resells long distance services to its residential and business customers and Eschelon has extensive experience with long distance resale. The companies anticipate that customers will experience a seamless transition of service provider. Further, these customers will be sufficiently notified of the Transaction and their rights. Hence, the public interest will be served by BPS's provision of services to the transferred GEBPS customers.

In sum, grant of this Application will serve the public interest by furthering competition in the Tennessee telecommunications market, as a result of the strengthened competitive position of Eschelon. Applicants desire to complete the proposed transaction by December 31, 2004. To that end, Applicants respectfully request that the Authority expedite the processing and grant of approval of this Application as soon as possible.

VIII. CONCLUSION

The Applicants respectfully request that the Authority grant approval for the transfer of substantially all of the assets, including the customers, of GE Business Productivity Solutions, Inc. to Business Productivity Solutions, Inc. Applicants further request that the Authority approve the transfer of GEBPS's authorization to BPS and the adoption of GEBPS's tariff by BPS effective as of *December 31, 2004*, and GEBPS's request to abandon service once its

customers have been fully transferred to BPS. Applicants respectfully request that the Authority grant all relief requested herein, and any additional relief the Authority determines is appropriate, on or before December 31, 2004.

Respectfully submitted,



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Counsel for GE Business Productivity
Solutions, Inc. and Business Productivity
Solutions, Inc.

Dated: October 21, 2004

EXHIBIT A

Articles of Incorporation Business Productivity Solutions, Inc.

ARTICLES OF INCORPORATION
OF
BUSINESS PRODUCTIVITY SOLUTIONS, INC.

The undersigned, a natural person of full age, for the purpose of forming a corporation under Minnesota Statutes, Chapter 302A, adopts the following Articles of Incorporation:

ARTICLE I

NAME

The name of this corporation shall be Business Productivity Solutions, Inc..

ARTICLE II

REGISTERED OFFICE

The registered office of this corporation is located at 730 Second Avenue So., Suite 1200, Minneapolis, MN 55402.

ARTICLE III

INCORPORATOR

The name and address of the incorporator are:

Name

Address

Michael Donahue

730 Second Avenue South
Suite 1200
Minneapolis, MN 55402

ARTICLE IV

CAPITAL

The aggregate number of shares of stock which this corporation shall have the authority to issue is One Thousand (1,000) shares with a par value of One Cent (\$0.01) per share.

ARTICLE V

CLASSES AND SERIES OF STOCK

In addition to, and not by way of limitation of, the powers granted to the Board of Directors by Minnesota Statutes, Chapter 302A, the Board of Directors of this corporation shall have the power and authority to fix by resolution any designation, class, series, voting power, preference, right, qualification, limitation, restriction, dividend, time and price of redemption, and conversion right with respect to any stock of the corporation. Upon adoption of such resolution, a statement shall be filed with the Secretary of State in compliance with Section 302A.401, Minnesota Statutes, before the issuance of any shares for which the resolution creates rights or preferences not set forth in these Articles; provided, however, where the shareholders have received notice of the creation of shares with rights or preferences not set forth in the Articles before the issuance of the shares, the statement may be filed any time within one year after the issuance of the shares.

ARTICLE VI

SHAREHOLDER VOTING

No shareholder of this corporation shall be entitled to any cumulative voting rights.

The shareholders of the corporation shall take action by the affirmative vote of the holders of a majority of the shares present and entitled to vote, except where a larger proportion is required by law, these Articles of Incorporation or a shareholder control agreement.

ARTICLE VII

PREEMPTIVE RIGHTS

No shareholder of this corporation shall have any preferential, preemptive, or other rights of subscription to any shares of any class or series of stock of this corporation allotted or sold or to be allotted or sold, whether now or hereafter authorized, or to any obligations or securities convertible into any class or series of stock of this corporation.

ARTICLE VIII

BOARD OF DIRECTORS

The names and addresses of the members of the initial Board of Directors are:

<u>Name</u>	<u>Address</u>
Cliff D. Williams	730 Second Avenue So., Suite 1200 Minneapolis, MN 55402
Richard A. Smith	730 Second Avenue So., Suite 1200 Minneapolis, MN 55402

Geoffrey M. Boyd

730 Second Avenue So., Suite 1200
Minneapolis, MN 55402

ARTICLE IX

DIRECTOR LIABILITY

A director of the corporation shall not be personally liable to the corporation or its shareholders for monetary damages for breach of fiduciary duty as a director, except for (i) liability based on a breach of the duty of loyalty to the corporation or the shareholders; (ii) liability for acts or omissions not in good faith or that involve intentional misconduct or a knowing violation of law; (iii) liability based on the payment of an improper dividend or an improper repurchase of the corporation's stock under Minnesota Statutes, Section 302A.559, or on violations of federal or state securities laws; (iv) liability for any transaction from which the director derived an improper personal benefit; or (v) liability for any act or omission occurring prior to the date this Article IX becomes effective. If Minnesota Statutes, Chapter 302A, hereafter is amended to authorize the further elimination or limitation of the liability of directors, then the liability of a director of the corporation in addition to the limitation on personal liability provided herein, shall be limited to the fullest extent permitted by the amended Chapter 302A. Any repeal of this provision as a matter of law or any modification of this Article by the shareholders of the corporation shall be prospective only, and shall not adversely affect any limitation on the personal liability of a director of the corporation existing at the time of such repeal or modification.

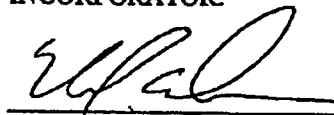
ARTICLE X

BOARD ACTION WITHOUT A MEETING

Any action required or permitted to be taken at any meeting of the Board of Directors may be taken without a meeting by written action signed by a majority of the members of the Board of Directors then in office, except as to those matters which require shareholder approval, in which case the written action shall be signed by all members of the Board of Directors then in office.

The incorporator has executed these Articles of Incorporation on October 6, 2004.

INCORPORATOR:



Michael A. Donahue

STATE OF MINNESOTA
DEPARTMENT OF STATE
FILED

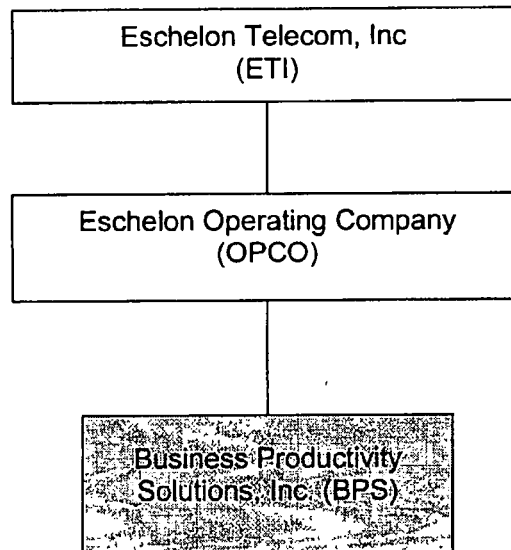
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Secretary of State

EXHIBIT B

Corporate Organizational Chart of Eschelon Post Transaction

CORPORATE OWNERSHIP STRUCTURE OF ESCHELON AFTER THE TRANSACTION*



* Each entity shown is 100% owned by the entity immediately above it. The shaded entities are the entities authorized to provide telecommunications services in Tennessee.

EXHIBIT C

Customer Notice



GE Business Productivity Solutions



IMPORTANT NOTICE REGARDING YOUR TELECOMMUNICATIONS SERVICES

Dear GE Business Productivity Solutions, Inc. Customer:

We are writing to share with you an exciting announcement regarding your GE Business Productivity Solutions, Inc. ("GEBPS") telecommunications services.

Recently, GEBPS and Eschelon Telecom, Inc. ("Eschelon") signed a definitive agreement whereby Eschelon will acquire the assets of GEBPS, including the GEBPS customers. The transaction is expected to become final on or around December 31, 2004, subject to customary regulatory approvals. Eschelon is an integrated communications provider of voice, data, Internet services and business telephone systems that serves over 38,000 customers. Eschelon is one of the fastest growing telecommunications companies in the nation and will continue to provide you with quality telecommunications services.

The combined company will bring together a wide range of expertise and resources while offering you the most complete line of high-quality, cost-effective products and services available. We will continue to support you with a team of highly-trained associates who will provide best-in-class customer service.

How will this affect your rates and services?

As stated above, we anticipate that the transfer of the GEBPS customers will take place on or around December 31, 2004. **Prior to and immediately following the transfer, you will continue to receive the same services at the same rates, terms and conditions as you do now.** After the transaction has completed, your service will automatically be transferred to Eschelon's telecommunications subsidiary, Business Productivity Solutions, Inc. ("BPS"). You will not be charged any fees in connection with this transfer. Notice of any future changes in rates, terms and conditions of service will be provided to you as required by law. Of course, at any time you are free to select a new service provider. If, however, you have a term contract with GEBPS, you will still be responsible for any applicable early termination charges.

What are the next steps?

You don't have to do a thing! We will notify you after the transaction has been completed. We are confident that you will be completely satisfied with BPS and will receive the same high level of customer service and support that you have come to expect.

Please note. If you have placed a "freeze" on your GEBPS services to prevent an unauthorized transfer to another carrier, it will be automatically lifted to implement the transfer to Eschelon and BPS. At your request, BPS can reestablish freeze protection for you after the transfer.

We will do everything to help ensure that this transition is a smooth one. If you would like to see a copy of GEBPS's rates and charges, please visit GEBPS's website at www.bizproductivity.com. If you have any questions or concerns regarding rates, billing statements, service needs, complaints or about the transfer of your service to BPS, please contact GEBPS Customer Service at **1-800-775-4322**. We look forward to updating you on the progress of this transaction. We will provide additional details regarding invoice descriptions, contact information and remittance addresses as we approach the transfer date.

Thank you,

GE Business Productivity Solutions, Inc.

Eschelon Telecom, Inc.

EXHIBIT D

Consolidated Financial Statements SEC Form 10-Q for Echelon Telecom, Inc.

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D C 20549-0001

FORM 10-Q

(MARK ONE)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2004

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

Commission File Number 000-50706

ESCHELON TELECOM, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

41 - 1843131
(I R S Employer
Identification No)

730 Second Avenue
Minneapolis, MN
(Address of principal executive offices)

55402
(Zip Code)

Registrant's telephone number, including area code (612) 376-4400

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to the filing requirements for the past 90 days Yes ☒ No ☐

Indicate by check mark whether the registrant is an accelerated filer as defined in Rule 12b-2 of the Exchange Act Yes ☐ No ☒

As of August 10, 2004, the number of outstanding shares of the Registrant's Common Stock, par value \$ 01 per share, was 4,665,964 shares and the number of outstanding shares of the Registrant's Preferred Stock, par value \$ 01 per share, was 84,306,677 shares, convertible into 99,732,467 shares of Common Stock

ESCHELON TELECOM, INC.
INDEX TO FORM 10-Q

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PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**

Eschelon Telecom, Inc.
Consolidated Balance Sheets
(In Thousands, Except Share and Per Share Amounts)

	December 31, 2003	June 30, 2004 (Unaudited)
Assets		
Current assets		
Cash and cash equivalents	\$ 8,606	\$ 23,843
Accounts receivable, net of allowance for doubtful accounts of \$739 and \$445, respectively	13,537	12,106
Other receivables	2,097	3,177
Inventories	3,169	3,141
Prepaid expenses	2,046	2,155
Total current assets	29,455	44,422
Property and equipment, net	86,777	85,966
Other assets	1,269	1,392
Goodwill	7,168	7,168
Intangible assets, net	29,052	29,678
Total assets	\$ 153,721	\$ 168,626
Liabilities and stockholders' equity (deficit)		
Current liabilities		
Accounts payable	\$ 4,582	\$ 6,140
Accrued telecommunication costs	6,939	6,876
Accrued expenses	3,240	6,264
Deferred revenue	3,000	3,720
Accrued compensation expenses	4,261	3,399
Capital lease obligation, current maturities	1,020	521
Total current liabilities	23,042	26,920
Long-term liabilities		
Commitments and contingencies (Note 3)		
Capital lease obligation	576	1,552
Notes payable	86,226	85,332
Total liabilities	109,844	113,804
Series A convertible preferred stock, \$0.01 par value, 100,000,000 shares authorized, 84,306,677 shares outstanding at December 31, 2003 and June 30, 2004	48,948	50,656
Stockholders' equity (deficit)		
Common stock, \$0.01 par value, 160,000,000 shares authorized, 4,457,579 shares issued and outstanding at December 31, 2003, and 4,665,964 shares issued and outstanding at June 30, 2004	45	47
Additional paid-in capital	120,105	118,413
Accumulated deficit	(125,167)	(114,260)
Deferred compensation	(54)	(34)
Total stockholders' equity (deficit)	(5,071)	4,166
Total liabilities and stockholders' equity (deficit)	\$ 153,721	\$ 168,626

See accompanying notes

Eschelon Telecom, Inc
Unaudited Consolidated Statements of Operations
(In Thousands, Except Share and Per Share Amounts)

	Three months ended June 30,		Six months ended June 30,	
	2003	2004	2003	2004
Revenue				
Network services	\$ 28,188	\$ 32,745	\$ 54,842	\$ 64,857
Business telephone systems	7,217	6,406	12,477	12,490
Total revenue	35,405	39,151	67,319	77,347
Cost of revenue				
Network services	11,184	11,592	21,849	23,357
Business telephone systems	4,189	3,818	7,556	7,480
Total cost of revenue	15,373	15,410	29,405	30,837
Gross profit				
Network services	17,004	21,153	32,993	41,500
Business telephone systems	3,028	2,588	4,921	5,010
Total gross profit	20,032	23,741	37,914	46,510
Operating expenses				
Sales, general and administrative	16,148	17,084	31,596	33,506
Depreciation and amortization	8,056	7,277	15,705	15,212
Operating loss	(4,172)	(620)	(9,387)	(2,208)
Other income (expense)				
Interest income	55	26	147	38
Interest expense	(448)	(2,760)	(879)	(5,074)
Gain on extinguishment of debt	—	—	—	18,195
Other expense	(36)	(23)	(106)	(44)
Income (loss) before taxes	(4,601)	(3,377)	(10,225)	10,907
Income taxes	—	—	—	—
Net income (loss)	(4,601)	(3,377)	(10,225)	10,907
Less preferred stock dividends	(854)	(854)	(1,699)	(1,708)
Net income (loss) applicable to common stockholders	\$ (5,455)	\$ (4,231)	\$ (11,924)	\$ 9,199
Net income (loss) per share				
Basic	\$ (1.76)	\$ (1.09)	\$ (4.33)	\$ 2.45
Diluted	\$ (1.76)	\$ (1.09)	\$ (4.33)	\$ 0.16
Weighted average number of shares outstanding				
Basic	3,101,923	3,889,854	2,750,800	3,759,693
Diluted	3,101,923	3,889,854	2,750,800	108,475,277

See accompanying notes

Eschelon Telecom, Inc
Unaudited Consolidated Statements of Cash Flows
(In Thousands)

	Six months ended June 30,	
	2003	2004
Operating activities		
Net income (loss)	\$ (10,225)	\$ 10,907
Adjustments to reconcile net income (loss) to net cash provided by operating activities		
Depreciation and amortization expense	15,705	15,212
Other non-cash items	1,067	1,409
Gain on extinguishment of debt	—	(18,195)
Changes in operating assets and liabilities		
Accounts receivable	(2,734)	987
Inventories	(478)	28
Other current assets and deposits	516	(1,312)
Accounts payable and accrued expenses	1,596	4,519
Deferred revenue	511	720
Accrued compensation expense	(670)	(862)
Net cash provided by operating activities	5,288	13,413
Investing activities		
Purchases of property and equipment	(8,019)	(6,979)
Cash paid for customer installation costs	(6,037)	(5,494)
Net cash used in investing activities	(14,056)	(12,473)
Financing activities		
Proceeds from issuance of notes payable	—	84,813
Payments made on bank debt and capital lease obligations	(1,503)	(66,299)
Proceeds from (fees associated with) issuance of stock	(62)	3
Increase in debt issuance costs	(58)	(4,220)
Net cash provided by (used in) financing activities	(1,623)	14,297
Net increase (decrease) in cash and cash equivalents	(10,391)	15,237
Cash and cash equivalents at beginning of period	19,733	8,606
Cash and cash equivalents at end of period	\$ 9,342	\$ 23,843
Supplemental cash flow information		
Cash paid for interest	\$ 232	\$ 4,167
Supplemental noncash activities		
Equipment purchases under capital leases	\$ 710	\$ 1,354
Value of common stock issued to management	\$ 124	\$ 14

See accompanying notes

Eschelon Telecom, Inc.
Notes to Consolidated Financial Statements
(In Thousands, Except Share and Per Share Amounts)
(Unaudited)

1.) Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited consolidated financial statements of Eschelon Telecom, Inc. and its subsidiaries (the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X promulgated by the United States Securities and Exchange Commission (the "SEC"). Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal and recurring adjustments and accruals) considered necessary for a fair presentation for the periods indicated have been included. Operating results for the three and six month periods ended June 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. The consolidated balance sheet at December 31, 2003 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. These financial statements should be read in conjunction with the Company's audited financial statements and related notes thereto for the year ended December 31, 2003 included in the Eschelon Operating Company Form S-4/A, File No. 333-114437-08, filed with the Securities and Exchange Commission on May 6, 2004.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Property and Equipment

Property and equipment, including leasehold improvements, are stated at cost. All internal costs directly related to the construction of the switches and operating and support systems, including salaries of certain employees, are capitalized. Depreciation is provided using the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized over the shorter of the related lease term or the estimated useful life of the asset.

Property and equipment consist of the following:

	December 31, 2003	June 30, 2004
Vehicles	\$ 39	\$ 121
Office furniture and equipment	13,243	14,566
Computer equipment and software	30,264	31,965
Leasehold improvements	16,931	17,287
Switching and data equipment and software	76,751	81,338
	137,228	145,277
Less accumulated depreciation	(50,451)	(59,311)
	<u>\$ 86,777</u>	<u>\$ 85,966</u>

Goodwill and Intangibles

Goodwill represents the excess of cost over the fair value of net assets acquired.

Intangibles consist of debt issuance costs, customer installation costs, and noncompete agreements. Debt issuance costs are being amortized over the term of the respective debt obligation. The customer installation costs are being amortized over a period of 48 months, which approximates the average life of a customer contract. Noncompete agreement costs represent costs associated with various agreements the Company has entered into with existing management of the companies they have acquired. These costs are being amortized over the terms of the agreements.

Intangible assets consist of the following:

	December 31, 2003	June 30, 2004
Customer set-up costs	\$ 52,794	\$ 58,290
Debt issuance costs	5,833	4,220
Non-compete agreements	15	15
	58,642	65,525
Less accumulated amortization	(29,590)	(32,847)
	\$ 29,052	\$ 29,678

Revenue Recognition

Revenues from network services are recognized in the period in which subscribers use the related services. Revenues from equipment sales and related installation charges are recognized upon delivery, completion of the installation of the related equipment, and acceptance by the customer, at which point legal title passes to the customer. Revenues for carrier interconnection and access are recognized in the period in which the service is provided.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Stock-Based Compensation

The Company accounts for its stock-based employee compensation under the recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations. Under APB No. 25, when the exercise price of stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized in the consolidated statement of operations.

The following table illustrates the effect on net income (loss) per share if the company had applied the fair value recognition provision of Statement of Financial Accounting Standards (SFAS) No. 123, *Accounting for Stock-Based Compensation*, to stock-based employee compensation.

	Three months ended June 30,		Six months ended June 30,	
	2003	2004	2003	2004
Net income (loss) applicable to common stockholders, as reported	\$ (5,455)	\$ (4,231)	\$ (11,924)	\$ 9,199
Add Stock-based employee compensation expense included in reported net income (loss)	—	—	70	20
Deduct Total stock-based employee compensation expense determined under fair value-based methods for all awards	(4)	(16)	(131)	(48)
Pro forma net income (loss) applicable to common stockholders	\$ (5,459)	\$ (4,247)	\$ (11,985)	\$ 9,171
Net income (loss) per share				
Basic - as reported	\$ (1.76)	\$ (1.09)	\$ (4.33)	\$ 2.45
Basic - pro forma	\$ (1.76)	\$ (1.09)	\$ (4.36)	\$ 2.44
Diluted - as reported	\$ (1.76)	\$ (1.09)	\$ (4.33)	\$ 0.16
Diluted - pro forma	\$ (1.76)	\$ (1.09)	\$ (4.36)	\$ 0.16

Pro forma information regarding net income (loss) and net income (loss) per share is required by SFAS No. 123, and has been determined as if the Company had accounted for its employee stock options under the fair value method of SFAS No. 123. The fair value of these options was estimated at the date of grant using the Black-Scholes option pricing model with the following assumptions for the three months ended June 30, 2003 and 2004: a risk-free interest rate of 3.25% and 3.88%, respectively, dividend yield of 0% for each period, volatility factor of the expected market price of the Company's common stock of 25% for each period, and a weighted average life of the options of five years for each period. The following assumptions were used for the six months ended June 30, 2003 and 2004: a risk-free interest rate ranging from 3.25% to 3.88%, dividend yield of 0% for each period, volatility factor of the expected market price of the Company's common stock of 25% for each period, and a weighted average life of the options of five years for each period.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions. Because the Company's employee stock options have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

Net Income (Loss) Per Share

Basic earnings per share is computed based on the weighted average number of common shares outstanding. Diluted earnings per share is computed based on the weighted average number of common shares outstanding adjusted by the number of additional shares that would have been outstanding had the potentially dilutive common shares been issued. Potentially dilutive shares of common stock include stock options, unvested restricted stock grants and Series A Convertible Preferred Stock. During periods in which a net loss is incurred, diluted earnings per share amounts are the same as basic per share amounts because the effect of all options, unvested restricted stock grants and Series A Convertible Preferred Stock is anti-dilutive.

The following table presents a reconciliation of the numerators and denominators of basic and diluted earnings per common share:

	Three months ended June 30,		Six months ended June 30,	
	2003	2004	2003	2004
Numerator				
Net income (loss) applicable to common stockholders, as reported	\$ (5,455)	\$ (4,231)	\$ (11,924)	\$ 9,199
Add: Cumulative preferred stock dividends	—	—	—	7,835
Deduct: Unrecognized deferred compensation expense	—	—	—	(34)
Numerator for diluted earnings per share	\$ (5,455)	\$ (4,231)	\$ (11,924)	\$ 17,000
Denominator				
Weighted average number of common shares outstanding	3,101,923	3,889,854	2,750,800	3,759,693
Effect of dilutive securities	—	—	—	426,810
Restricted stock grants	—	—	—	4,556,306
Employee stock options	—	—	—	99,732,468
Series A convertible preferred stock	—	—	—	—
Denominator for diluted earnings per share	3,101,923	3,889,854	2,750,800	108,475,277
Net income (loss) per share				
Basic - as reported	\$ (1.76)	\$ (1.09)	\$ (4.33)	\$ 2.45
Diluted - as reported	\$ (1.76)	\$ (1.09)	\$ (4.33)	\$ 0.16

New Accounting Pronouncements

In May 2003, the Financial Accounting Standards Board issued SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity*. SFAS No. 150 requires that certain financial instruments, which under previous guidance were accounted for as equity, must now be accounted for as liabilities. The financial instruments affected include mandatorily redeemable stock, certain financial instruments that require or may require the issuer to buy back some of its shares in exchange for cash or other assets and certain obligations that can be settled with shares of stock. SFAS No. 150 is effective for all financial instruments entered into or modified after May 31, 2003, and otherwise is effective the beginning of the first interim period after June 15, 2003. The adoption of SFAS No. 150 did not have a material impact on the Company's financial statements and did not require the Company to reclassify its Series A Preferred Stock to a liability as the shares are contingently redeemable.

Reclassifications

Certain prior year amounts have been reclassified to conform to current year presentation.

2.) Notes Payable

In March 2004, the Company completed an offering of \$100,000 of 8 3/8% senior second secured notes due 2010 at a discount resulting in a 12% yield. Proceeds from the offering were used to retire bank debt with a principal balance of \$65,421, pay fees related to the offering and provide additional liquidity to the Company.

The carrying value of notes payable is comprised of the following:

	December 31, 2003	June 30, 2004
Principal balance due	\$ 64,355	\$ 100,000
Excess carrying value	21,871	—
Discount on note payable	—	(14,668)
Carrying value	\$ 86,226	\$ 85,332

3.) Commitments and Contingencies

In April 2003, the Company entered into a five-year agreement with MCI to purchase colocation/LIS transport services. The agreement requires that the Company maintain monthly minimums as follows:

April 2004-March 2005	\$ 84/month
April 2005-March 2006	\$ 88/month
April 2006-March 2007	\$ 93/month
April 2007-March 2008	\$ 97/month

The Company will pay an underutilization charge for any amounts billed under the monthly minimum.

In 2000, the Company entered into an amendment of an earlier Master Purchase and Service agreement with Nortel Networks, Inc. (Nortel Networks). Under the amendment, the Company committed to purchase and/or license \$100,000 of Nortel Networks' equipment or services. However, the Company is confident that, due to Nortel Networks' discontinuance of certain product lines contemplated in the Amended Master Purchase and Services agreement, neither party will be held to the conditions of the contract.

In August 2000, the Company entered into a ten-year agreement with Global Crossing to purchase a total of \$100,000 of services. The agreement does not contain monthly minimums, however a penalty is assessed for early termination upon change in control. Upon change in control, the early termination penalties are \$10,000 through August 2004, and \$5,000 from September 2004 through August 2010.

See Regulatory Overview and Legal Proceedings discussion within the Management's Discussion and Analysis and Legal Proceedings sections presented in this document.

4.) Capital Stock

Under the terms of the Series A Convertible Preferred Stock, the holders are entitled to receive, when and if declared by the Board of Directors, cumulative dividends on each share of the Series A Convertible Preferred Stock at a rate of 8% per year which shall accrue daily and, to the extent not paid, shall accumulate quarterly in arrears. At December 31, 2003 and June 30, 2004, dividends in arrears are \$6,127 and \$7,835, respectively.

The shares of Series A Convertible Preferred Stock, plus all accrued and unpaid dividends at the time of conversion, are convertible at any time, at the option of the holder, into shares of the Company's common stock at the initial conversion price, which is the original issue price of \$0.5079. The conversion price is subject to adjustment in the event of certain events, such as dilutive issuances of additional securities. The Series A Convertible Preferred Stock will automatically convert into common stock in the event of an initial public offering raising at least the greater of \$50,000 or the amount of principal and interest outstanding under the Credit Agreement. The Series A Convertible Preferred Stock may be automatically converted upon the consent of the holders of at least 60% of the then outstanding shares of Series A Convertible Preferred Stock.

The shares of Series A Convertible Preferred Stock will be redeemed on the tenth anniversary of the original issuance, if the shares have not previously been redeemed or converted. The Company may redeem all of the Series A Convertible Preferred Stock upon the effectiveness of an initial public offering. The redemption price of the Series A Convertible Preferred stock will be the greater of (i) the original issue price plus all accrued and unpaid dividends or (ii) the fair market value of the shares of common stock, as determined by the Board of Directors, that would be received upon conversion of (a) the Series A Convertible Preferred Stock, and (b) any accrued and unpaid dividends on the Series A Convertible Preferred Stock. Upon a change of control, the holders of 60% of the then outstanding shares of the Series A Convertible Preferred Stock may require the Company to redeem all of or a portion of the Series A Convertible Preferred Stock at a price equal to (1) the liquidation preference (as described below) if the change of control occurs before the fifth anniversary of the original issue date and (2) the redemption price if the change of control occurs after the fifth anniversary of the original issue date.

In the event of the Company's liquidation, the holders of the Series A Convertible Preferred Stock will receive any distribution of corporate assets before any distributions are made to a junior class of equity. The amount to be distributed to the holders of Series A Convertible Preferred Stock will be the greater of (i) two times the original issue price plus all accrued and unpaid dividends (whether or not yet accumulated) as of the date of distribution, or (ii) the fair market value of the shares of the Company's common stock, as determined by the Board of Directors, that would be received upon (1) conversion of the Series A Convertible Preferred Stock, (2) any accrued and unpaid dividends and, (3) if the liquidation is prior to the fifth anniversary of the date of issuance of the Series A Convertible Preferred Stock, all additional dividends that would have been accrued through the fifth anniversary date.

Stock Options

In November 2002, the Board of Directors approved the Eschelon Telecom, Inc. Stock Option Plan of 2002 (the 2002 Plan). A total of 14,117,647 shares of the Company's common stock have been reserved for issuance under the 2002 Plan. At June 30, 2004, the Company had 10,337,796 options outstanding and 2,484,979 shares of restricted common stock issued to certain directors and members of management under the 2002 Plan.

Restricted Common Stock

In February 2003, the Company granted 2,484,979 shares of restricted common stock to certain directors and members of management. The fair value per share of this restricted stock was \$0.05. The Company records compensation expense as the restrictions are removed from the stock. In February 2003, 1,399,902 shares had vested resulting in compensation expense related to restricted common stock of \$70. In February 2004, an additional 405,968 shares had vested resulting in compensation expense of \$20.

Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking and Cautionary Statements

We make "forward-looking statements" throughout this document. Whenever you read a statement that is not solely a statement of historical fact (such as when we state that we "may," "will" or "plan to" perform in a certain manner or that we "intend," "believe," "expect," "anticipate," "estimate" or "project" that an event will occur, or the negative thereof, and other similar statements), you should understand that our expectations may not be correct, although we believe that they are reasonable. You should also understand that our plans may change. We do not guarantee that the transactions and events described in this document will happen as described or that any positive trends noted in this document will continue.

Forward-looking statements, such as those regarding management's present plans or expectations for new product offerings, capital expenditures, cost-saving strategies and growth are not guarantees of future performance. They involve risks and uncertainties relative to return expectations and related allocation of resources, and changing economic or competitive conditions, as well as the negotiation of agreements with third parties and other factors discussed herein, which could cause actual results to differ from present plans or expectations, and such differences could be material. Similarly, forward-looking statements regarding management's present expectations for operating results and cash flow involve risks and uncertainties relative to these and other factors, such as the ability to increase revenues and/or to achieve cost reductions and other factors discussed herein, which also would cause actual results to differ from present plans. Such differences could be material. All forward-looking statements attributable to us or by any persons acting on our behalf are expressly qualified in their entirety by these cautionary statements.

As such, actual results or circumstances may vary materially from such forward-looking statements or expectations. Readers are also cautioned not to place undue reliance on these forward-looking statements which speak only as of the date these statements were made. Except as required by law, we will not update these forward-looking statements, even if our situation changes in the future.

Company Overview

We are a leading facilities-based provider of integrated voice and data communications services to small and medium-sized businesses in 12 markets in the western United States. Our voice and data services, which we refer to as network services, include local dial tone, long distance, enhanced voice features and dedicated Internet access services. We also sell, install and maintain business telephone and data systems and equipment, which we call BTS. We provide these products and services individually or in customized packages to address our customers' need for an outsourced voice and data network solution.

We have increased our annual revenue every year from \$41.7 million for the year ended December 31, 1999 to \$141.1 million for the year ended December 31, 2003, and we have increased our gross profit from \$14.8 million to \$80.3 million over the same period. As of June 30, 2004, we provided service through 225,949 total access lines, an increase of 9.5% from 206,421 total access lines at December 31, 2003.

Our goal is to provide services to our customers on our network, or on-net, which will allow us to continue to expand our operating margins and improve profitability. We have continued to increase the percentage of on-net customers with a strategically deployed and incentivized sales force. Increasing our on-net percentage improves customer retention, leverages our network, increases profitability and reduces our exposure to regulatory risk. We selectively provide service via the unbundled network element-platform, or UNE-P, to reach locations outside of our network footprint of on-net customers and to provide Qwest DSL. For the six months ended June 30, 2004, 89.1% of our new access lines installed were on-net and as of June 30, 2004, 77.4% of our total access lines in service were on-net.

Customer retention is a key metric that we use to measure the success of our business. We report monthly access line attrition, or churn, as measured by dividing total access lines disconnected for the month by our total access lines at the end of the month. We believe our low level of churn reflects our high quality of service and the value proposition we provide to new and existing customers. Due to our focus on improved service levels, competitive pricing and customer credit quality, we have reduced our monthly churn to levels that we believe are industry leading. For the six months ended June 30, 2004, our monthly churn averaged 1.53% compared to 1.60% for the year ended December 31, 2003.

Revenue. Network services revenue consists primarily of local dial tone, long distance, access charges, and data service. Revenue from local telephone service consists of charges for basic local service, including dedicated T1 access, and custom-calling features such as call waiting and call forwarding. Revenue from long distance service consists of per-minute-of-use charges for a full range of traditional switched and dedicated long distance, toll-free calling, international, calling card and operator services. Revenue from data services consists primarily of monthly usage fees for dedicated Internet access services.

Network services revenue is recognized in the month the services are used. In the case of local service revenue, local services charges are billed in advance but accrued for and recognized on a prorated basis based on length of service in any given month. Long distance and access charges are billed in arrears but accrued based on monthly average usage per line per day. We do not receive any revenues from reciprocal compensation due to our bill-and-keep arrangement with Qwest nor do we have any wholesale revenue other than access revenue. For the six month period ended June 30, 2004, carrier access revenue represented 8.5% of our total revenue.

BTS revenue consists of revenue from both the sale of telephone equipment and the servicing of telephone equipment systems. Telephone equipment revenue is recognized upon delivery and acceptance by the customer. Service revenue is recognized upon completion of service or, in the case of maintenance agreements, is spread equally over the life of the maintenance contract.

Cost of revenue. Our network services cost consists primarily of the cost of operating and maintaining our network facilities. The network components for our facilities-based business include the cost of:

- leasing local loops and digital T1 lines which connect our customers to our network,
- leasing high capacity digital lines that interconnect our network with ILECs,
- leasing high capacity digital lines that connect our switching equipment to our colocations,
- leasing space in ILEC central offices for collocating our equipment,
- signaling system network connectivity, and
- leasing our ATM backbone network.

The costs to lease local loops, digital T1 lines and high capacity digital interoffice facilities from the ILECs varies by carrier and by state and are regulated under the Telecommunications Act of 1996. In virtually all areas, we lease local loops, T1 lines and interoffice capacity from the ILECs. We lease interoffice facilities from carriers other than the ILEC where possible in order to lower costs and improve network redundancy. However, in most cases, the ILEC is the only source for local loops and T1 lines. We also purchase, on a wholesale or negotiated basis, UNE-P and customized network element packages, or UNE-E, from Qwest and Centrex services from SBC Communications Inc. The rates for UNE-P and Centrex are regulated and established by the various state corporation or utility commissions. As of June 30, 2004 and December 31, 2003, we had 42,921 and 45,041 UNE-P access lines in service, respectively. As of June 30, 2004 and December 31, 2003, we had 8,095 and 8,493 Centrex access lines in service, respectively. The rates for UNE-E were negotiated with Qwest under the terms of a five-year contract that expires December 31, 2005. As of June 30, 2004 and December 31, 2003, we had 1,942 and 1,934 UNE-E access lines in service, respectively.

We have entered into wholesale purchasing agreements with long distance and other service providers. Some of these agreements also contain termination penalties and/or minimum usage volume commitments. In the event we fail to meet minimum volume commitments, we may be obligated to pay underutilization charges. We do not anticipate having to pay any underutilization charges in the foreseeable future.

We carefully review all of our vendor invoices and frequently dispute inaccurate or inappropriate charges. Our single largest vendor is Qwest, to whom we paid \$25.8 million for the year ended December 31, 2003, and \$16.7 million for the six months ended June 30, 2004. We frequently short pay vendor invoices in order to pay proper amounts owed. We use significant estimates to determine the level of success in dispute resolution and consider past historical experience, basis of dispute, financial status and current relationship with vendors and aging of prior disputes in quantifying our estimates.

We account for all of our network depreciation in depreciation and amortization expense and do not have any depreciation in cost of revenue.

Our most significant BTS costs are the equipment purchased from manufacturers and labor for service and equipment installation. To take advantage of volume purchase discounts, we purchase equipment primarily

from three manufacturers. For BTS installations our policy is to require a 30% deposit before ordering the equipment so our risk of excess inventory or inventory obsolescence is low. BTS cost of revenue also includes salaries and benefits of field technicians as well as vehicle and incidental expenses associated with equipment installation, maintenance and service provisioning.

Sales, general and administrative expenses Sales, general and administrative expenses are comprised primarily of salaries and benefits, bonuses, commissions, occupancy costs, sales and marketing expenses, bad debt, billing and professional services.

Determining our allowance for doubtful accounts receivable requires significant estimates. We consider a number of factors in determining the proper level of the allowance, including historical collections experience, current economic trends, the aging of the accounts receivable portfolio and changes in the creditworthiness of our customers. We perform a rigorous credit review process on each new customer that involves reviewing the customer's current service provider bill and payment history, matching customers with the National Telecommunications Data Exchange database for delinquent customers and, in some cases, requesting credit reviews through Dun and Bradstreet. For the six months ended June 30, 2003 and 2004, our bad debt expense as a percentage of revenue was 0.5% and 0.6%, respectively.

Depreciation and amortization Our depreciation and amortization currently includes depreciation for network related voice and data equipment, back office systems, furniture, fixtures, leasehold improvements, office equipment and computers. All internal costs directly related to the expansion of our network and operating and support systems, including salaries of certain employees, are capitalized and depreciated over the lives of the switches or systems, as the case may be. Capitalized customer installation costs are amortized over the approximate average life of a customer. Detailed annual time studies are used to determine labor capitalization. These time studies are based on employee time sheets for those engaged in capitalizable activities.

In 2002, we adopted Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Intangible Assets*. SFAS No. 142 provides that goodwill and intangible assets that have indefinite useful lives not be amortized but rather be tested at least annually for impairment.

Regulatory Overview

FCC rules implementing the local competition provisions of the Telecommunications Act permit CLECs to lease UNEs at rates determined by PUCs employing the FCC's Total Element Long Run Incremental Cost, or TELRIC, forward-looking, cost-based pricing model. On September 15, 2003, the FCC opened a proceeding re-examining the TELRIC methodology and wholesale pricing rules for communications services made available for resale by ILECs in accordance with the Telecommunications Act. This proceeding will comprehensively re-examine whether the TELRIC pricing model produces unpredictable pricing inconsistent with appropriate economic signals, fails to adequately reflect the real-world attributes of the routing and topography of an ILEC's network, and creates disincentives to investment in facilities by understating forward-looking costs in pricing RBOC network facilities and overstating efficiency assumptions. We have joined a coalition of CLECs to participate in this proceeding. The application and effect of a revised TELRIC pricing model on the communications industry generally and on certain of our business activities cannot be determined at this time.

In August 2003, in its TRO, the FCC substantially modified its rules governing access to UNEs by CLECs. However, on March 2, 2004, the D.C. Circuit vacated certain portions of the TRO and remanded the TRO to the FCC for further proceedings. Specifically, the Court vacated the FCC's delegation of decision-making authority to state commissions and several of the FCC's nation-wide impairment determinations. The Court also found that the FCC used a flawed methodology when making certain network element unbundling determinations and remanded those determinations back to the FCC for further analysis and justification. The Court temporarily stayed the effectiveness of its decision until (1) the denial of any petition for rehearing or (2) May 2, 2004. The Court subsequently extended the effective date until June 15, 2004.

The FCC and the Solicitor General have declined to appeal the Court's order. The National Association of Regulatory Utility Commissioners and a coalition of CLECs, including Eschelon, separately appealed the decision. We expect to learn whether the Supreme Court will take the case before the end of the year.

Although the Court's order is now in effect, we do not know how or when the FCC will respond to it. The FCC could issue interim rules in a relatively short time period that would remain in effect until permanent rules were issued or the FCC could forego interim rules. We do not know when the FCC might issue either interim or permanent rules nor do we know what the rules will be or the effect such rules could have upon our business. However, it has been reported in the trade press that the FCC will shortly issue a Notice of Proposed Rulemaking that will "preserve rates for unbundled network elements for six months, with rate increases expected to occur in the months that follow, according to industry sources." It is speculated that a notice of proposed rulemaking to establish permanent rules will be released that calls for grandfathering any lines in service as of the end of the standstill period at total-element long-run increment cost (TELRIC) rates plus a 15% increase. It is further speculated that the [Notice] would open the door for ILECs to set the rates for new network access orders, subject to contractual obligations⁽¹⁾.

The ILECs have stated that they interpret the order as eliminating unbundled switching, transport, high capacity loops and dark fiber as UNEs. Except for dark fiber, Eschelon uses all of these UNEs. Eschelon, along with many other CLECs, interprets the effect of the order differently, reasoning that under the 1996 Telecommunications Act as well as under state statutes, unbundling is still required where CLECs are impaired without access to UNEs. Furthermore, whereas the Court explicitly vacated the rules requiring the unbundling of mass market switching and transport, it was silent with respect to high capacity loops.

The ILECs have also stated that they will follow the "change of law" provisions in our interconnection agreements. These provisions provide that when a party to the agreement believes the governing law has changed its obligations under the agreement, it may request that the other party enter into negotiations to amend the agreement. If the parties are unable to agree upon an amendment, the dispute is arbitrated either by a neutral arbitrator or by the relevant state commission. We anticipate that "change of law" negotiations will commence soon. We do not know when the negotiations might conclude nor the effect of any amendments arrived at upon our business.

The FCC has encouraged ILECs and CLECs to engage in commercial negotiations to provide access to ILEC facilities that may no longer be available as UNEs. Although a few such agreements have been announced, the great majority of CLECs, including Eschelon, have not succeeded in negotiating new agreements as of this date. Qwest and MCI recently made public a four-year agreement which provides MCI an alternative to the UNE-P products they currently purchase from Qwest today at higher prices. Qwest has stated that it will make similar terms and conditions available to other CLECs. We are currently evaluating the agreement. In addition, Eschelon has sent Qwest its own proposal relating to UNE-P, but we have not yet received a response.

As a condition of entering the long distance markets, the Act requires ILECs to provide CLECs with loops, transport, and unbundled switching. In the TRO, the FCC determined, and the D.C. Circuit Court agreed, that these facilities must be made available to CLECs at "just and reasonable" rates, in contrast to UNEs which are available at TELRIC rates. We do not know what "just and reasonable" rates would be nor do we know when such rates might be established nor the roles of the FCC or state commissions in establishing such rates. In addition, Bell South has petitioned the FCC requesting that the FCC forbear from requiring RBOCs to provide an element under the long distance provisions of the Act if the RBOC is no longer required to provide the analogous UNE under the local competition portions of the Act. We do not know how the FCC will rule on Bell South's petition.

(1) "Interim UNE Rules Expected To Offer Six-Month Freeze, Could Spark Bell Legal Fight," *Telecommunications Reports* August 1, 2004.

Comparison of Financial Results

Overview of Results

Selected consolidated financial and operating data for the three and six month periods ended June 30, 2003 and 2004 is as follows (dollars in thousands, except per unit amounts)

	Three months ended June 30,			Six months ended June 30,		
	2003 (unaudited)	2004 (unaudited)	% Change	2003 (unaudited)	2004 (unaudited)	% Change
Total revenue	\$ 35,405	\$ 39,151	10.6%	\$ 67,319	\$ 77,347	14.9%
Total gross margin (%)	56.6%	60.6%	7.2%	56.3%	60.1%	6.8%
EBITDA	\$ 3,884	\$ 6,657	71.4%	\$ 6,318	\$ 13,004	105.8%
Capital expenditures	\$ 8,054	\$ 6,789	(15.7)%	\$ 14,776	\$ 13,829	(6.4)%
Cash	\$ 9,342	\$ 23,843	155.2%	\$ 9,342	\$ 23,843	155.2%
Voice lines in service	144,396	162,622	12.6%	144,396	162,622	12.6%
Data lines in service	36,825	63,327	72.0%	36,825	63,327	72.0%
Total lines in service	181,221	225,949	24.7%	181,221	225,949	24.7%
Lines on-net (%)	69.6%	77.4%	11.3%	69.6%	77.4%	11.3%
Lines sold	20,889	22,773	9.0%	43,866	42,236	(3.7)%
Average monthly churn (%)	1.71%	1.52%	(10.9)%	1.75%	1.53%	(12.1)%
Average network revenue per line	\$ 52.98	\$ 49.06	(7.4)%	\$ 53.22	\$ 49.73	(6.6)%
Average total associates	890	918	3.1%	898	902	0.4%
Average total sales associates	189	195	3.2%	190	184	(3.2)%
Average network sales associates	152	156	2.9%	153	148	(3.5)%

Three Months Ended June 30, 2004 versus Three Months Ended June 30, 2003

Revenue Revenue for the three months ended June 30, 2003 and 2004 is as follows

	2003 (unaudited)	2004 (unaudited)	% Change
Revenue (in millions):			
Voice and data services	\$ 20.4	\$ 24.1	18.3%
Long distance	4.7	5.4	13.8%
Access	3.1	3.3	5.6%
Total network services	28.2	32.8	16.2%
Business telephone systems	7.2	6.4	(11.2)%
Total revenue	\$ 35.4	\$ 39.2	10.6%

Network services revenue was \$32.8 million for the three months ended June 30, 2004, an increase of 16.2% from \$28.2 million in the same period of 2003. The increase in revenue was primarily due to an increase in the average number of voice and data access lines in service. Over the past 12 months the number of voice lines increased by 12.6% to 162,622 lines at June 30, 2004 and the number of data lines increased by 72.0% to 63,327 lines at June 30, 2004. The growth in access lines was partially offset by declines in long distance and access revenue per minute of use and a decline in data revenue per line. Due to continued high levels of competition, long distance revenue per minute of use declined. Access revenue per minute of use declined in line with the scheduled FCC reduction of interstate rate levels. Data revenue per line declined due to a combination of customers purchasing more bandwidth at discounted prices and general pricing pressures for data services in our markets. We expect all of the above trends in line growth, long distance rates, access rates and data revenue per line to continue for the foreseeable future. As we continue to grow, our size and churn will begin to limit our access line growth rate on both an absolute and on a percentage basis unless we increase our sales force and geographic territory.

BTS revenue was \$6.4 million for the three months ended June 30, 2004, a decrease of 11.2% from \$7.2 million in the same period of 2003. The decrease in revenue was primarily due to a decrease in revenue from change orders and new system sales. We cannot predict future trends in capital spending by small and medium-sized business customers.

Cost of Revenue. Cost of revenue for the three months ended June 30, 2003 and 2004 is as follows:

	2003 (unaudited)	2004 (unaudited)	% Change
Cost of revenue (in millions):			
Network services	\$ 11.2	\$ 11.6	3.6%
Business telephone systems	\$ 4.2	\$ 3.8	(8.9)%
Total cost of revenue	\$ 15.4	\$ 15.4	0.2%

Network services cost of revenue was \$11.6 million for the three months ended June 30, 2004, an increase of 3.6% from \$11.2 million in the same period of 2003. This increase is due to our growth in access lines. As a percentage of related revenue, network services cost of revenue for the three months ended June 30, 2004 declined to 35.4% from 39.7% for the same period of 2003. This improvement was due to the increase in our percentage of access lines on-net to 77.4% as of June 30, 2004 from 69.6% as of June 30, 2003.

BTS cost of revenue was \$3.8 million for the three months ended June 30, 2004, a decrease of 8.9% from \$4.2 million in the same period of 2003. This decrease was due to a decrease in materials cost related to the change orders and new system sales mentioned previously. As a percentage of related revenue, BTS cost of revenue for the three months ended June 30, 2004 increased to 59.6% from 58.0% for the same period of 2003. We do not expect future improvements in BTS cost of revenue as a percentage of related revenue unless we are able to significantly increase BTS revenue and therefore achieve greater volume discounts or economies of scale in our workforce.

Gross Profit. Gross profit for the three months ended June 30, 2003 and 2004 is as follows:

	2003 (unaudited)	2004 (unaudited)	% Change
Gross profit (in millions):			
Network services	\$ 17.0	\$ 21.2	24.4%
Business telephone systems	\$ 3.0	\$ 2.6	(14.5)%
Total gross profit	\$ 20.0	\$ 23.8	18.5%

The increase in gross profit for the three months ended June 30, 2004, from the same period of 2003, is due to the increase in revenue mentioned previously.

Sales, General and Administrative Expense. Sales, general and administrative expenses were \$17.1 million for the three months ended June 30, 2004, an increase of 5.8% from \$16.1 million in the same period of 2003. The increase is primarily due to higher average payroll and fringe benefit expenses and an increase in operating taxes. As a percentage of revenue, sales, general and administrative expenses for the three months ended June 30, 2004 declined to 43.6% from 45.6% in the same period of 2003 due to the improved efficiency of our existing operations resulting from our fixed cost structure supporting a higher level of revenue. We expect this trend to continue as we add more access lines with only modest increase in our employee base.

EBITDA. Earnings before interest, taxes, depreciation and amortization (EBITDA) was \$6.7 million for the three months ended June 30, 2004, an increase of 71.4% from \$3.9 million in the same period of 2003. This increase was due to increased profit margins and lower sales, general and administrative expenses as a percentage of revenue.

EBITDA is not a measure of financial performance under generally accepted accounting principles (GAAP). EBITDA is provided because it is a measure of financial performance commonly used as an indicator of a company's historical ability to service debt. EBITDA should not be construed as an alternative to operating income, as an indicator of operating performance nor as an alternative to cash flows provided by operating activities as a measure of liquidity determined in accordance with GAAP. We may

calculate EBITDA differently than other companies. The following is a schedule reconciling EBITDA with reported GAAP net income (loss) for the three months ended June 30, 2003 and 2004 (dollars in thousands)

	2003 (unaudited)	2004 (unaudited)
EBITDA	\$ 3,884	\$ 6,657
Depreciation and amortization	(8,056)	(7,277)
Interest expense	(448)	(2,760)
Loss on disposal of assets	(36)	(23)
Interest income	55	26
Net income (loss)	\$ (4,601)	\$ (3,377)

Depreciation and Amortization. Depreciation and amortization expense was \$7.3 million for the three months ended June 30, 2004, a decrease of 9.7% from \$8.1 million in the same period of 2003. This decrease was primarily due to accelerated depreciation in 2003 on the abandonment of our previous billing system per SFAS No. 144. As a percentage of revenue, depreciation and amortization decreased to 18.6% for the three months ended June 30, 2004 from 22.8% for the same period of 2003.

Interest. Interest expense was \$2.8 million for the three months ended June 30, 2004, an increase of 516.4% from \$0.4 million in the same period of 2003. This increase was primarily due to interest expense on our senior second secured notes.

Six Months Ended June 30, 2004 versus Six Months Ended June 30, 2003

Revenue. Revenue for the six months ended June 30, 2003 and 2004 is as follows:

	2003 (unaudited)	2004 (unaudited)	% Change
Revenue (in millions)			
Voice and data services	\$ 39.5	\$ 47.6	20.6%
Long distance	9.2	10.7	15.9%
Access	6.1	6.6	7.1%
Total network services	54.8	64.9	18.3%
Business telephone systems	12.5	12.5	0.1%
Total revenue	\$ 67.3	\$ 77.4	14.9%

Network services revenue was \$64.9 million for the six months ended June 30, 2004, an increase of 18.3% from \$54.8 million in the same period of 2003. The increase in revenue was primarily due to an increase in the average number of voice and data access lines in service. Over the past 12 months the number of voice lines increased by 12.6% to 162,622 lines at June 30, 2004, and the number of data lines increased by 72.0% to 63,327 lines at June 30, 2004. The growth in access lines was partially offset by declines in long distance and access revenue per minute of use and a decline in data revenue per line. Due to continued high levels of competition, long distance revenue per minute of use declined. Access revenue per minute of use declined in line with the scheduled FCC reduction of interstate rate levels. Data revenue per line declined due to a combination of customers purchasing more bandwidth at discounted prices and general pricing pressures for data services in our markets. We expect all of the above trends in line growth, long distance rates, access rates and data revenue per line to continue for the foreseeable future. As we continue to grow, our size and churn will begin to limit our access line growth rate on both an absolute and on a percentage basis unless we increase our sales force and geographic territory.

BTS revenue was \$12.5 million for each of the six months ended June 30, 2003 and 2004. We cannot predict future trends in capital spending by small and medium-sized business customers.

Cost of Revenue Cost of revenue for the six months ended June 30, 2003 and 2004 is as follows

	2003 (unaudited)	2004 (unaudited)	% Change
Cost of revenue (in millions)			
Network services	\$ 21.8	\$ 23.3	6.9%
Business telephone systems	7.6	7.5	(1.0)%
Total cost of revenue	\$ 29.4	\$ 30.8	4.9%

Network services cost of revenue was \$23.3 million for the six months ended June 30, 2004, an increase of 6.9% from \$21.8 million in the same period of 2003. This increase is due to our growth in access lines. As a percentage of related revenue, network services cost of revenue for the six months ended June 30, 2004 declined to 36.0% from 39.8% for the same period of 2003. This improvement was due to the increase in our percentage of access lines on-net to 77.4% as of June 30, 2004 from 69.6% as of June 30, 2003.

BTS cost of revenue was \$7.5 million for the six months ended June 30, 2004, a decrease of 1.0% from \$7.6 million in the same period of 2003. As a percentage of related revenue, BTS cost of revenue for the six months ended June 30, 2004 decreased to 59.9% from 60.6% for the same period of 2003. We do not expect future improvements in BTS cost of revenue as a percentage of related revenue unless we are able to significantly increase BTS revenue and therefore achieve greater volume discounts or economies of scale in our workforce.

Gross Profit Gross profit for the six months ended June 30, 2003 and 2004 is as follows

	2003 (unaudited)	2004 (unaudited)	% Change
Gross profit (in millions)			
Network services	\$ 33.0	\$ 41.5	25.8%
Business telephone systems	4.9	5.0	1.8%
Total gross profit	\$ 37.9	\$ 46.5	22.7%

The increase in gross profit for the six months ended June 30, 2004, from the same period of 2003, is due to the increase in revenue mentioned previously.

Sales, General and Administrative Expense. Sales, general and administrative expenses were \$33.5 million for the six months ended June 30, 2004, an increase of 6.0% from \$31.6 million in the same period of 2003. The increase is primarily due to higher average payroll, fringe benefit and sales recruiting expenses and an increase in operating taxes. As a percentage of revenue, sales, general and administrative expenses for the six months ended June 30, 2004 declined to 43.3% from 46.9% in the same period of 2003 due to the improved efficiency of our existing operations resulting from our fixed cost structure supporting a higher level of revenue. We expect this trend to continue as we add more access lines with only modest increase in our employee base.

EBITDA. Earnings before interest, taxes, depreciation and amortization (EBITDA) was \$13.0 million for the six months ended June 30, 2004, an increase of 105.8% from \$6.3 million in the same period of 2003. This increase was due to increased profit margins and lower sales, general and administrative expenses as a percentage of revenue.

The following is a schedule reconciling EBITDA with reported GAAP net income (loss) for the six months ended June 30, 2003 and 2004 (dollars in thousands)

	2003 (unaudited)	2004 (unaudited)
EBITDA	\$ 6,318	\$ 13,004
Depreciation and amortization	(15,705)	(15,212)
Interest expense	(879)	(5,074)
Deferred compensation	(70)	(20)
Loss on disposal of assets	(36)	(24)
Interest income	147	38
Gain on debt restructuring		18,195
Net income (loss)	\$ (10,225)	\$ 10,907

Depreciation and Amortization. Depreciation and amortization expense was \$15.2 million for the six months ended June 30, 2004, a decrease of 3.1% from \$15.7 million in the same period of 2003. This decrease was primarily due to accelerated depreciation in 2003 on the abandonment of our previous billing system per SFAS No. 144. As a percentage of revenue, depreciation and amortization decreased to 19.7% for the six months ended June 30, 2004 from 23.3% for the same period of 2003.

Interest. Interest expense was \$5.1 million for the six months ended June 30, 2004, an increase of 477.2% from \$0.9 million in the same period of 2003. This increase was primarily due to interest expense on our senior second secured notes and a \$1.6 million prepayment penalty associated with the prepayment of our bank facility.

Gain on Extinguishment of Debt. Net income for the six months ended June 30, 2004 included a gain on extinguishment of debt of \$18.2 million. The gain on the extinguishment of debt was the result of paying off our bank facility. In June 2002, we restructured our bank facility and because the future cash flows could not be calculated with certainty, the gain was deferred. As a result of the repayment, the excess carrying value of \$20.9 million and debt issuance costs of \$2.7 million resulted in the \$18.2 million gain on extinguishment of debt.

Liquidity and Capital Resources

Financings. In March 2004, we completed an offering of \$100 million of 8 3/8% senior second secured notes due 2010 at a discount resulting in a 12% yield. We used the proceeds from our offering to retire bank debt, pay fees related to the offering and provide additional liquidity to our company. After repayment of our senior secured bank facility and fees related to the issuance of the new notes, we received incremental cash of approximately \$13.6 million.

Cash Flows Provided by Operating Activities. Cash provided by operating activities was \$13.4 million for the six months ended June 30, 2004 compared to cash provided by operating activities of \$5.3 million for the six months ended June 30, 2003. Our improvement in cash provided by operating activities was primarily due to our growth in gross profit accompanied by a smaller increase in our operating expenses. Working capital improved primarily through improvement in our accounts receivable collections and an increase in our accounts payable days outstanding. Average accounts receivable days sales outstanding improved from 35.0 for the six months ended June 30, 2003 to 30.9 for the six months ended June 30, 2004. Average accounts payable days outstanding increased from 68.0 for the six months ended June 30, 2003 to 78.3 for the six months ended June 30, 2004. We do not expect further improvement in our accounts receivable or accounts payable days outstanding in the future.

Cash Flows Used in Investing Activities. Cash used in investing activities was \$12.5 million for the six months ended June 30, 2004 compared to \$14.1 million for the six months ended June 30, 2003. The cash used in investing activities was primarily for the maintenance and expansion of our network and back office systems.

Cash Flows Provided by (Used in) Financing Activities. Cash provided by financing activities was \$14.3 million for the six months ended June 30, 2004. The net proceeds from the issuance of the senior second secured notes generated approximately \$13.6 million, which is net of a \$1.6 million prepayment penalty mentioned previously. For the six months ended June 30, 2003, net cash used in financing activities was \$1.6 million, primarily for payment on capital lease obligations.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are not exposed to market risks from changes in foreign currency exchange rates or commodity prices. We do not hold any derivative financial instruments nor do we hold any securities for trading or speculative purposes.

We are exposed to changes in interest rates on our investments in cash equivalents and short-term investments. All of our investments are in cash equivalents with maturities of less than three months which reduces our exposure to long-term interest rate changes. Interest income for the three and six month periods ended June 30, 2004 was \$26.4 thousand and \$37.5 thousand, respectively, therefore not exposing us to any meaningful interest income risk had rates dropped. Excluding capital leases, we had \$85.3 million in senior second secured notes outstanding as of June 30, 2004. These notes are at a fixed interest rate and are therefore not exposed to any interest rate risk.

Item 4. Controls and Procedures

Based on their evaluation as of the end of the period covered by this Quarterly Report on Form 10-Q, our principal executive officer and principal financial officer with the participation and assistance of our management, concluded that our disclosure controls and procedures, as defined in Rules 13a-15(e) promulgated under the Securities Exchange Act of 1934, were effective in design and operation. There have been no significant changes in our system of internal controls or in other factors that could significantly affect internal controls subsequent to the date of their evaluation.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On August 2, 2004, a Nevada state court entered a judgment against Eschelon for intentionally interfering with a former salesperson's economic relationship with his new employer in the amount of \$376 thousand plus costs. We had reason to believe the former employee was violating his non-solicitation agreement with us. We are considering appealing the judgment because, among other reasons, the jury was not instructed to consider whether we were justified in informing the new employer of the agreement and our intent to enforce it.

We are a party to several complaint proceedings against Qwest filed with the Arizona, Colorado, Minnesota and Washington public utility commissions, or PUCs, and two federal court lawsuits involving Qwest. The Minnesota PUC recently ordered Qwest to pay us approximately \$500 thousand as a refund of overcharges related to enhanced extended loops and Qwest may appeal the order. We have appealed the recent unfavorable decisions by the Minnesota PUC in relation to our complaints regarding Qwest's withholding of Direct Measures of Quality, or DMOQ billing credits and our request for a refund from Qwest for overcharges for our colocations. The Minnesota PUC and the Arizona Corporation Commission recently granted, and the Washington PUC denied in part and granted in part, our complaints regarding retroactive application of certain favorable UNE rates. We have filed a similar complaint in Colorado. We continue to pursue a lawsuit against Qwest in the United States District Court, Western District of Washington regarding the financial harm we have suffered as a result of Qwest's violations of our interconnection agreements by failing to provide accurate records relating to interstate and intrastate long distance calls, failing to develop an unbundled network platform and failing to make DSL available for resale. We also are opposing Qwest's federal court appeal of the Minnesota PUC's UNE Cost Order. If Qwest is successful, our UNE rates in Minnesota could increase.

We are a party to certain regulatory investigations underway in Arizona, Colorado and Washington relating to the alleged failure of Qwest and several CLECs, including us, to submit interconnection agreements for approval by state regulatory agencies. We cannot predict the outcome of the Arizona, Colorado or Washington investigations or the effect that any corresponding regulatory actions may have on our business. A similar investigation by the Minnesota PUC resulted in no direct penalties against us. The Minnesota Department of Commerce has filed a complaint with the Minnesota PUC concerning agreements that CLECs, including us, have with certain interexchange carriers for pricing access services. They have asserted that the agreements are unlawfully discriminatory and required to be filed.

We cannot predict the outcome of any of these proceedings or their effect on our business.

Item 2. Changes in Securities, Use of Proceeds and Issuer Purchase of Equity Securities

On March 17, 2004, Eschelon Operating Company (a wholly owned subsidiary) issued \$100 million principal amount at maturity of 8 3/8% Senior Second Secured Notes due in 2010. Jefferies & Company, Inc. and Wachovia Securities were the joint book-running managers for the transaction. These notes were priced at 84.813% of the principal amount and the gross proceeds were \$84.813 million.

We offered these notes to qualified institutional buyers as defined in Rule 144A under the Securities Act, to persons outside the United States under Regulation S of the Securities Act and to a limited number of institutional accredited investors within the meaning of Rule 501 (a) (1), (2), (3) or (7) of the Securities Act. An exchange offer with the holders of the notes, whereby the notes were exchanged for a like principal amount of registered 8 3/8% Senior Second Secured Notes due 2010, was completed on June 18, 2004.

The proceeds of this transaction were used to repay existing indebtedness of \$65.4 million and to pay \$5.8 million of associated fees and expenses of the offering. The remaining \$13.6 million of proceeds is being used for general corporate purposes.

We relied upon Rule 701 promulgated under the Securities Act to issue the following securities:

On March 15, 2004, we granted to 186 participants under the Eschelon Telecom, Inc. Stock Option Plan of 2002 options to purchase an aggregate of 277,617 shares of common stock at an exercise price of \$0.10 per share. These options generally vest 20% upon the date of the initial grant and 20% per year over four years from the date of grant.

On May 20, 2004, we granted to 417 participants under the Eschelon Telecom, Inc. Stock Option Plan of 2002 options to purchase an aggregate of 986,817 shares of common stock at an exercise price of \$0.10 per share. These options generally vest 20% upon the date of the initial grant and 20% per year over four years from the date of grant.

On May 20, 2004, we issued to two independent members of our Board of Directors 140,365 shares of common stock at a price of \$0.10 per share as compensation for Board duties.

Item 3 Defaults Upon Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of the security holders during the quarter ended June 30, 2004.

Item 5 Other Information

None

Item 6. Exhibits and Reports on Form 8-K

a) Exhibits

Exhibit No	Description
3.1*	Fifth Amended and Restated Certificate of Incorporation of Eschelon Telecom, Inc. filed on June 27, 2002
3.2*	By-Laws of Eschelon Telecom, Inc.
4.1*	Fourth Amended and Restated Stockholders Agreement dated June 27, 2002
4.2*	Eschelon Telecom, Inc. 2002 Stock Incentive Plan
4.3*	Form of Incentive Stock Option Grant Agreement Under the Eschelon Telecom, Inc. 2002 Stock Incentive Plan
4.4*	Form of Nonstatutory Stock Option Grant Agreement Under the Eschelon Telecom, Inc. 2002 Stock Incentive Plan
4.5*	Form of Restricted Stock Grant Agreement Under the Eschelon Telecom, Inc. 2002 Stock Incentive Plan
4.6**	Indenture dated March 17, 2004 by and among Eschelon Operating Company, Eschelon Telecom, Inc., Eschelon Telecom of Minnesota, Inc., Eschelon Telecom of Washington, Inc., Eschelon Telecom of Colorado, Inc., Eschelon Telecom of Nevada, Inc., Eschelon Telecom of Utah, Inc., Eschelon Telecom of Oregon, Inc., Eschelon Telecom of Arizona, Inc., and The Bank of New York Trust Company, N.A.
4.7**	Registration Rights Agreement dated March 17, 2004 by and among Jefferies & Company, Inc., Wachovia Capital Markets LLC, Eschelon Operating Company, Eschelon Telecom, Inc., Eschelon Telecom of Minnesota, Inc., Eschelon Telecom of Washington, Inc., Eschelon Telecom of Colorado, Inc., Eschelon Telecom of Nevada, Inc., Eschelon Telecom of Utah, Inc., Eschelon Telecom of Oregon, Inc., and Eschelon Telecom of Arizona, Inc.
4.8**	Security Agreement dated March 17, 2004 by and among Eschelon Operating Company, Eschelon Telecom, Inc., Eschelon Telecom of Minnesota, Inc., Eschelon Telecom of Washington, Inc., Eschelon Telecom of Colorado, Inc., Eschelon Telecom of Nevada, Inc., Eschelon Telecom of Utah, Inc., Eschelon Telecom of Oregon, Inc., Eschelon Telecom of Arizona, Inc., and The Bank of New York Trust Company, N.A. (as Collateral Agent)
4.9**	Trademark Security Agreement dated March 17, 2004 by and among Eschelon Operating Company, Eschelon Telecom, Inc., and The Bank of New York Trust Company, N.A. (as Collateral Agent)
4.10**	Form of Initial 8 3/8% Senior Second Secured Notes due 2010
4.11**	Form of Guarantee of Initial 8 3/8% Senior Second Secured Notes due 2010
4.12**	Form of Exchange 8 3/8% Senior Second Secured Notes due 2010
4.13**	Form of Guarantee of Exchange 8 3/8% Senior Second Secured Notes due 2010
10.1*	Change-in-Control Severance Pay and Employment Agreement dated November 22, 2002 by and between Eschelon Telecom, Inc. and Richard A. Smith
10.2*	Employment Offer Letter dated March 7, 2000 from Eschelon Telecom, Inc. to Geoffrey M. Boyd
10.2.1*	Severance Pay Letter Agreement dated November 14, 2002 by and between Eschelon Telecom, Inc. and Geoffrey M. Boyd
10.4*	Employment Offer Letter dated July 19, 1999 from Eschelon Telecom, Inc. to Steven K. Wachter

- 10 5* Stock Restriction Agreement dated February 7, 2003 between Eschelon Telecom, Inc and Marvin C Moses
- 10 6* Stock Restriction Agreement dated February 7, 2003 between Eschelon Telecom, Inc and Anthony J Cassara
- 10 7* Stock Restriction Agreement dated February 7, 2003 between Eschelon Telecom, Inc and Peter M Van Genderen
- 10 8* Carrier Global Services Agreement dated July 28, 2000 by and between MCI WorldCom Communications, Inc and Eschelon Telecom, Inc
- 10 8 1* First Amendment dated June 20, 2001 to Carrier Global Services Agreement dated July 28, 2000 by and between MCI WorldCom Communications, Inc and Eschelon Telecom, Inc
- 10 8 2* Second Amendment dated April 8, 2002 to Carrier Global Services Agreement dated July 28, 2000 by and between MCI WorldCom Communications, Inc and Eschelon Telecom, Inc
- 10 8 3* Third Amendment dated April 1, 2003 to Carrier Global Services Agreement dated July 28, 2000 by and between MCI WorldCom Communications, Inc and Eschelon Telecom, Inc
- 10 8 4* WorldCom Internet Dedicated Service Agreement and Service Order Form dated June 12, 2003
- 10 8 5* WorldCom Internet Dedicated Service Agreement and Service Order Form dated January 23, 2004
- 10 8 6* WorldCom Internet Dedicated T3 Price-Protected Agreement dated July 26, 2001
- 10 8 7* WorldCom Wholesale Dedicated Internet Pricing Sheet
- 10 9* Carrier Service Agreement dated August 25, 2000 between Global Crossing Bandwidth, Inc. and Eschelon Telecom, Inc
- 10 9 1* Amendment #1 dated November 10, 2000 to Carrier Service Agreement dated August 25, 2000 between Global Crossing Bandwidth, Inc and Eschelon Telecom, Inc
- 10 9 2* Amendment #2 dated January 2, 2001 to Carrier Service Agreement dated August 25, 2000 between Global Crossing Bandwidth, Inc and Eschelon Telecom, Inc
- 10 9 3* Amendment #3 dated June 25, 2001 to Carrier Service Agreement dated August 25, 2000 between Global Crossing Bandwidth, Inc and Eschelon Telecom, Inc
- 10 9 4* Amendment #4 dated July 17, 2001 to Carrier Service Agreement dated August 25, 2000 between Global Crossing Bandwidth, Inc and Eschelon Telecom, Inc
- 10 9 5* Amendment #5 dated April 25, 2002 to Carrier Service Agreement dated August 25, 2000 between Global Crossing Bandwidth, Inc and Eschelon Telecom, Inc
- 10 9 6* Amendment #6 dated July 12, 2002 to Carrier Service Agreement dated August 25, 2000 between Global Crossing Bandwidth, Inc and Eschelon Telecom, Inc
- 10 9 7* Amendment #7 dated March 26, 2004 to Carrier Service Agreement dated August 25, 2000 between Global Crossing Bandwidth, Inc and Eschelon Telecom, Inc
- 10 10* Advisory Agreement dated March 15, 2004 among Eschelon Telecom, Inc, Bain Capital Investors, LLC, Wind Point Advisor, L L C, and Stolberg, Meehan & Scano, L L C
- 10 11* Lease of Office Space by and between St Paul Properties, Inc and Eschelon Telecom, Inc dated as of November 18, 2003
- 10 12* Lease Agreement by and between Timeshare Systems, Inc and Advanced Telecommunications, Inc dated March 3, 1999
- 10 13* Lease For Storage dated July 30, 1996 by and between T H S Northstar Associates Limited Partnership and Fishnet com, Inc
- 10 13 1* First Amendment dated March 10, 1998 of Lease for Storage dated July 30, 1996 by and between T H S Northstar Associates Limited Partnership and Fishnet com, Inc
- 10 13 2* Second Amendment dated March 27, 1998 of Lease for Storage dated July 30, 1996 by and between T H S Northstar Associates Limited Partnership and Fishnet com, Inc
- 10 13 3* Third Amendment dated April 30, 1999 of Lease for Storage dated July 30, 1996 by and between T H S Northstar Associates Limited Partnership and Fishnet com, Inc
- 10 13 4* Fourth Amendment dated October 3, 2000 of Lease for Storage dated July 30, 1996 by and between T H S Northstar Associates Limited Partnership and Fishnet com, Inc
- 10 13 5* Lease For Storage dated March 6, 2000 by and between T H S Northstar Associates Limited Partnership and Fishnet com, Inc
- 10 13 6* Lease For Storage dated July 11, 1999 by and between T H S Northstar Associates Limited Partnership and Fishnet com, Inc

- 10 14* Lease Agreement by and between Duke Realty Limited Partnership and Cady Communications, Inc. dated May 21, 1999
- 10 15* Lease Agreement between Seattle Telecom LLC and Advanced Telecommunications, Inc. dated December 20, 1999
- 10 16* Office Lease by and between Parkside Salt Lake Corporation and Advanced Telecommunications, Inc. dated December 28, 1999
- 10 17* Lease by and between Denver Place Associates Limited Partnership and Eschelon Telecom of Colorado, Inc. dated October 24, 2000
- 10 18* Office Lease by and between SOFI-IV SIM Office Investors II, Limited Partnership and Advanced Telecommunications, Inc. dated December 19, 1999
- 10 18 1* First Amendment dated March 17, 2003 to Lease by and between SOFI-IV SIM Office Investors II, Limited Partnership and Eschelon Telecom, Inc. dated December 19, 1999
- 10 19* Lease by and between Alco Investment Company and Advanced Telecommunications, Inc. dated November 19, 1999
- 21 1* Subsidiaries of Eschelon Telecom, Inc.
- 31 1 Certification by Richard A. Smith, Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31 2 Certification by Geoffrey M. Boyd, Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32 1 Certification by Richard A. Smith, Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32 2 Certification by Geoffrey M. Boyd, Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Incorporated herein by reference to Eschelon Telecom, Inc. Registration Statement on Form 10, No. 000-50706

** Incorporated herein by reference to Eschelon Operating Company Registration Statement on Form S-4, No. 333-114437

b) Reports on Form 8-K

On June 10, 2004, Eschelon Operating Company (a wholly owned subsidiary) filed a Form 8-K containing the press release issued on June 10, 2004 announcing the extension of our exchange offer.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized

Eschelon Telecom, Inc

Date August 11, 2004

By. /S/ Geoffrey M. Boyd

Name Geoffrey M. Boyd
Title Chief Financial Officer
(Principal Financial and
Accounting Officer and Duly
Authorized Officer)

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Certifications

I, Richard A. Smith, certify that

1 I have reviewed this quarterly report on Form 10-Q of Eschelon Telecom, Inc ,

2 Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report,

3 Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report,

4 The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e)) for the registrant and have

- a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared,
- b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about effectiveness of the disclosure controls and procedures, as of the end of period covered by this report based on such evaluation, and
- c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of a annual report) that has materially affected, or reasonably likely to materially affect, the registrant's internal control over financial reporting, and

5 The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions)

- a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information, and
- b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's control over financial reporting

August 11, 2004

Sign /S/ Richard A. Smith
Richard A. Smith
President and Chief Executive Officer

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Certifications

I, Geoffrey M Boyd, certify that

- 1 I have reviewed this quarterly report on Form 10-Q of Eschelon Telecom, Inc ,
- 2 Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report,
- 3 Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report,
- 4 The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e)) for the registrant and have
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared,
 - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about effectiveness of the disclosure controls and procedures, as of the end of period covered by this report based on such evaluation, and
 - c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of a annual report) that has materially affected, or reasonably likely to materially affect, the registrant's internal control over financial reporting, and
- 5 The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions)
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information, and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's control over financial reporting

August 11, 2004

Sign /s/ Geoffrey M Boyd
Geoffrey M Boyd
Chief Financial Officer

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**CERTIFICATION PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT
OF 2002 (18 U.S.C. SECTION 135)**

In connection with the Quarterly Report of Eschelon Telecom, Inc., a Delaware corporation (the "Company"), on Form 10-Q for the quarterly period ended June 30, 2004, as filed with the Securities and Exchange Commission (the "Report"), Richard A. Smith, Chief Executive Officer of the Company, does hereby certify, pursuant to § 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. § 1350), that to his knowledge

- (1) The report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, and
- (2) The information contained in the Report fairly represents, in all material respects, the financial condition and result of operations of the Company

Sign /s/ Richard A. Smith
Richard A. Smith
President and Chief Executive Officer
August 11, 2004

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**CERTIFICATION PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT
OF 2002 (18 U.S.C. SECTION 135)**

In connection with the Quarterly Report of Eschelon Telecom, Inc., a Delaware corporation (the "Company"), on Form 10-Q for the quarterly period ended June 30, 2004, as filed with the Securities and Exchange Commission (the "Report"), Geoffrey M. Boyd, Chief Financial Officer of the Company, does hereby certify, pursuant to § 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. § 1350), that to his knowledge

- (1) The report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, and
- (2) The information contained in the Report fairly represents, in all material respects, the financial condition and result of operations of the Company

Sign /s/ Geoffrey M. Boyd
Geoffrey M. Boyd
Chief Financial Officer
August 11, 2004

EXHIBIT E

Resumes of Senior Management of Eschelon Telecom, Inc.

Clifford Williams is Eschelon's Founder and Chairman of the Board. He also previously served as the Company's Chief Executive Officer from July 1996 to August 2003. From September 1995 to July 1996, Mr. Williams was raising capital for the formation of the Company. From March 1992 to September 1995, Mr. Williams was President and Chief Executive Officer of Enhanced Telemanagement Incorporated, an integrated communications provider that offered a full line of telecommunications products and services to small businesses in Minnesota, Washington, Oregon, Illinois and Ohio. From 1971 to 1991, Mr. Williams held a variety of senior management positions in the cable television industry, leading to Vice President and General Manager for Rogers Communications Inc. in Minneapolis. He also served as Vice President and General Manager for Rogers Communications Inc. in Toronto, Ontario.

Richard Smith serves as Eschelon's President and Chief Executive Officer. Smith joined Eschelon in October, 1998 as the Chief Financial Officer, was appointed to the Company's Board of Directors in July 2000, served as the Company's Chief Operating Officer from March 1999 through July 2003 and was elected President in April 2000. From April 1997 to October 1998, Mr. Smith served as Vice President of Financial Management for Frontier Corp. where he had been employed since 1972. Prior to serving in this role at Frontier, Mr. Smith held various positions including Controller, Chief Information Officer and President of Frontier Information Technologies, Vice President of Midwest Telephone Operations, Network Plant Operations Director and Director of Business Development. He also was a member of the Board of Directors of the Upstate Cellular Network - a joint venture between Frontier and NYNEX. Mr. Smith holds degrees in Electrical Technology from the Rochester Institute of Technology, Electrical Engineering from the State University of New York at Buffalo, Mathematics from the State University of New York at Brockport, and Business from the University of Rochester's Simon School. Smith has also published books on deregulation strategies and productivity for telecommunications companies.

Geoffrey Boyd Geoffrey Boyd has served as our Chief Financial Officer since March 2000. Prior to joining Eschelon, from September 1997 to March 2000 Mr. Boyd served in a variety of roles at Dobson Communications Corporation including Director of Mergers and Acquisitions and Strategic Planning and Chief Financial Officer of the company's CLEC subsidiary. Mr. Boyd started his career in banking, spending six years with Shawmut Bank and CoreStates in communications and media finance. He received a BA degree from Dartmouth College.

Robert Pickens joined Eschelon in April 1996 and serves as Executive Vice President of Marketing. Prior to joining Eschelon from July 1995 to March 1996 Mr. Pickens served as General Manager of Local Services and Operations for Frontier Corp. From June 1990 to June

1995 Mr. Pickens served as Marketing Manager and Marketing Director for ETI. Mr. Pickens received a BSB degree in Marketing with distinction from the University of Minnesota Carlson School of Management.

David Kunde has served as Executive Vice President of Engineering and Operations since July 2000. Prior to that, serving as Vice President of Operations and Technology Planning since joining the firm in May 1999. From 1994 until joining Eschelon, Mr. Kunde held the positions of Vice President of Network Engineering and Director of Network Engineering and Operations at Citizens Communications. From 1986 to 1994, Mr. Kunde held a variety of positions with Frontier Corp. (then Rochester Telephone). Mr. Kunde received a BA in Physics from Wittenberg University in Springfield, Ohio and a MBA from the University of Rochester's William E. Simon Graduate School.

Arlin Goldberg serves as Executive Vice President of Information Technology and joined the Company in October of 1996. Previously, Mr. Goldberg was the Director of Information Services at Frontier Corp. Prior to that, Mr. Goldberg was the Director of Information Services for ETI. Early in his career, Mr. Goldberg served in a variety of roles at Norstan. Mr. Goldberg received his BSB in Accounting from the University of Minnesota.

Steven Wachter has served as Executive Vice President of Sales and Service Delivery since August 1999. Prior to joining Eschelon, Mr. Wachter served in a variety of capacities at Ameritech Corporation since October 1994 including Director Business Sales - Wisconsin, East Region GM/Director - Small Business Marketplace, General Manager/Director - Premises Sales, and Director of Sales Programming. Mr. Wachter received a BS degree from the State University of New York at Geneseo Campus.

Carol Braun currently serves as the Company's Vice President of Human Resources. Prior to joining Eschelon in 1997, Ms. Braun held several accounting positions leading to Manager of Accounting, Finance and Human Resources with Cady Communications, Inc. which was acquired by Eschelon in July 1996. Ms. Braun received her BA from Concordia College - Moorhead, and has an MBA through the University of St. Thomas.

Michael Donahue serves as Vice President of Finance and Treasurer. Mr. Donahue joined the company in July 1996 as Vice President and Controller. Previously, Mr. Donahue was Division Controller at Frontier Corp. Prior to that, Mr. Donahue was the Director of Finance and Controller for ETI from November 1988 to July 1995. Mr. Donahue is a Certified Public Accountant and received his BS degree in Accounting and MBA in Finance from the University of Minnesota.

William Markert serves as Vice President - Network Financial Management. Mr. Markert joined Eschelon in January, 2000 as Director - Cost of Access. Prior to joining the company, Mr. Markert served in various financial analysis, accounting and management positions for Frontier Corp. Mr. Markert has a BS degree in Business Administration from the University of Wisconsin - Whitewater and an MBA from the University of St. Thomas.

Jeffery Oxley serves as Executive Vice President of Law and Policy and joined Eschelon in October, 1999. Prior to joining Eschelon, Mr. Oxley served as Assistant Attorney General for the state of Minnesota. Previously, Mr. Oxley was a product marketing manager at Oracle Corporation. Mr. Oxley has a BA degree in Economics from Stanford, an MA degree in Economics from Yale University and a JD degree from the University of Minnesota Law School, where he served as Editor-in-Chief of the Minnesota Law Review.

Michael Evans joined Eschelon in November 2002 as Vice President of Business Telephone System Operations. Prior to joining Eschelon, Mr. Evans spent over three years with XO Communications, most recently as the VP of Operations and Finance for the National Sales division in Dallas, Texas. From 1990 to 1999, Mr. Evans was employed by Frontier Corporation and held a variety of operations and finance positions with responsibilities in both network and equipment businesses (BTS) in Minnesota, Illinois and New York. From 1986 to 1990 he served in regulatory and controllership capacities with Universal Telephone in Milwaukee, Wisconsin. Prior to that, Mr. Evans was a senior auditor with PriceWaterhouseCoopers. Mr. Evans received a BA in Accounting from the University of Wisconsin - Oshkosh and is a Certified Public Accountant.

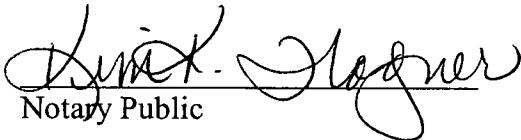
VERIFICATION

I, Jeffery Oxley, am Executive Vice President of Law and Policy of Eschelon Telecom, Inc. and am authorized to represent it and its subsidiaries, including Business Productivity Solutions, Inc., and to make this verification on their behalf. The statements in the foregoing document relating to this company and its subsidiaries, except as otherwise specifically attributed, are true and correct to the best of my knowledge and belief.

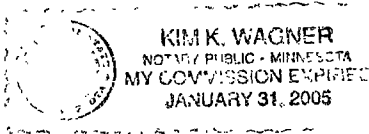
I declare under penalty of perjury that the foregoing is true and correct.



Subscribed and sworn to before me this 10th day of
October 2004.


Notary Public

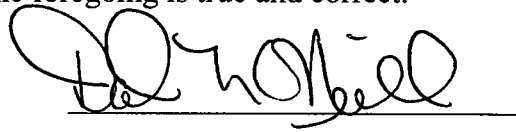
My Commission expires 1/31/05



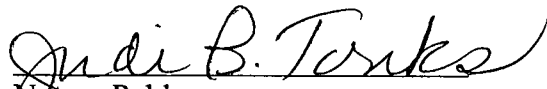
VERIFICATION

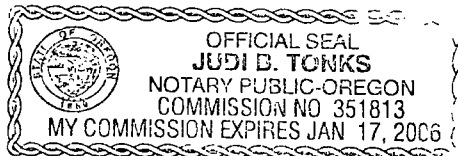
I, David M. O'Neill, am President of GE Business Productivity Solutions, Inc. and am authorized to represent it and to make this verification on its behalf. The statements in the foregoing document relating to this company, except as otherwise specifically attributed, are true and correct to the best of my knowledge and belief.

I declare under penalty of perjury that the foregoing is true and correct.



Subscribed and sworn to before me this 15 day of
October 2004.


Notary Public



My Commission expires: 1-17-2006